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CHARLES ELMORE CRO

Supreme Court of the United States

OCTOBER TERM, 1936.

No. 670

THE HARRIMAN NATIONAL BANK AND TRUST COMPANY OF THE CITY OF NEW YORK,

Petitioner,

—against—

HENRY E. OPPENHEIMER,

Respondent.

CROSS PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SECOND CIRCUIT AND BRIEF IN SUPPORT THEREOF.

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Counsel for Petitioner.

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Attorneys for the Comptroller of the Currency,
Of Counsel.

THE COURT PRESS, N. Y. C.

INDEX.

PAGE

Cross-Petition 1

Summary Statement of the Matter Involved..... 2

Reasons Relied on for the Allowance of the Writ.... 5

Brief 9

Opinion in the Court Below..... 9

Jurisdiction 9

Statement of the Case..... 9

Specification of Errors intended to be Urged..... 9

Summary of Argument..... 10

Argument:

I—The decision sought to be reviewed is erroneous because it directs that a claim founded upon the fraud of national bank officers in inducing the person defrauded to purchase shares of the bank's stock shall participate in the proceeds of an assessment collected from the other shareholders..... 11

II—The decision sought to be reviewed is erroneous because it compels petitioner, a national bank, to acquire and to pay for shares of its own capital stock in a manner unauthorized by Title 12, U. S. C., Section 83 (R. S. §5201), the only provision of law under which a national bank may acquire and hold shares of its own stock..... 21

PAGE

III—The decision sought to be reviewed is erroneous because it imposes liability upon a national bank for the fraud of its officers in connection with the sale of shares of its corporate stock which said shares were not sold from among its assets but were the property of another and it was not enriched by the transaction 28

Conclusion 32

Appendices A-G 33-38

TABLE OF CASES CITED:

Aicotin v. *Atlas Exchange Nat. Bank*, 295 U. S. 209..6, 27

Bradley v. *Harriman Nat. Bank & Trust Company*, 247 N. Y. App. Div. 876 (leave to appeal denied, 248 N. Y. App. Div. 564 and 271 N. Y. 663).....30-31

Burrows v. *Niblack*, 84 F. 111 (C. C. A. 7).....22-23

Clinton Mining & Mineral Co. v. *Beacom*, 266 F. 621 (C. C. A. 3) (cert. den. 254 U. S. 637).....19-21

East Broken Hills Consols., Ltd. v. *Mallaby-Deeley*, 11 T. L. R. 241, affd. id. 245..... 17

Farmers' State Guaranty Bank v. *Cromwell*, 70 Okla. 199, 173 Pac. 826..... 31

Goess v. *Ehret*, 13 F. Supp. 630 (affd. other grounds, 85 F. (2d) 109)..... 26

Heitman v. *Harriman*, 14 F. Supp. 282..... 31

Helburn Thompson Co. v. *All Americas Mercantile Corporation*, 211 N. Y. App. Div. 69..... 24

Houldsworth v. *City of Glasgow Bank & Liquidators*, 5 App. Cas. 317.....13, 14, 15

Hull & County Bank, In re, Burgess' Case, 15 C. H. Div. 507..... 16

PAGE

Jaskow v. *Harriman Nat. Bank & Trust Company*, 159 N. Y. Misc. 39 28-30

Lantry v. *Wallace*, 182 U. S. 536 ..... 5, 12
Lantry v. *Wallace*, 97 F. 865 5

Schechter v. *Sherwin*, 81 F. (2d) 603 (C. C. A. 7) 24
Scott v. *Deweese*, 181 U. S. 202 12
Smith v. *Tracy*, 36 N. Y. 79 31

U. S. v. *Bank of Columbus*, 21 How. 356 31
U. S. v. *Knox*, 102 U. S. 422 12

Wallace v. *Hood*, 89 F. 11 22

TABLE OF STATUTES CITED:

Companies Act, 1862 (25 and 26 Vict., p. 614) 13
Title 12 U. S. C. §24, subd. Seventh 26, 38
Title 12 U. S. C. §51 ..... 25, 35
Title 12 U. S. C. §51c 25, 36
Title 12 U. S. C. §53 ..... 25, 36
Title 12 U. S. C. §54 ..... 25, 37
Title 12 U. S. C. §56 23
Title 12 U. S. C. §59 ..... 23, 25
Title 12 U. S. C. §64 ..... 10, 11, 12, 18, 21
Title 12 U. S. C. §83 ..... 10, 21, 23, 27
Title 12 U. S. C. §191 ..... 12, 33
Title 12 U. S. C. §192 ..... 12, 33
Title 28 U. S. C. §347a (Judicial Code §240 [a] as amended by Act of February 13, 1925) 9

TABLE OF AUTHORITIES CITED:

Morse on Banks & Banking, 6th Ed., §132 31

Supreme Court of the United States

OCTOBER TERM, 1936.

No. .

THE HARRIMAN NATIONAL BANK AND TRUST COMPANY OF THE CITY OF NEW YORK,

Petitioner,

—against—

HENRY E. OPPENHEIMER,

Respondent.

Cross-Petition for a Writ of Certiorari to the United States Circuit Court of Appeals for the Second Circuit and Brief in Support thereof.

To the Honorable, the Chief Justice of the United States and the Associate Justices:

Your petitioner, The Harriman National Bank and Trust Company of the City of New York, a national banking association, now in receivership, by direction of the Comptroller of the Currency, respectfully prays that a writ of certiorari issue to review a resettled judgment of the United States Circuit Court of Appeals for the Second Circuit entered on November 9, 1936 in so far as the same reverses the judgment of the District Court in favor of petitioner and orders the entry of final judgment against petitioner for the amount demanded in the respondent's complaint (R. 178).*

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* All references are to pages of the record.

The respondent also has petitioned this Court for a review and modification of the said judgment of the Circuit Court of Appeals. Petitioner has not submitted any brief in opposition to that application for the reason that the considerations set forth in this cross-petition and brief establish that the respondent (petitioner upon that application) is not entitled to any relief.

I.

Summary Statement of the Matter Involved.

Action at law by respondent, as plaintiff, against the petitioner and Henry E. Cooper, conservator of petitioner, defendants.

Respondent on November 1, 1930 purchased 10 shares of petitioner's capital stock and received a certificate for the shares (R. 4-5).

The stock sold to respondent was not petitioner's property but the property of its affiliate, The Harriman Securities Corporation, and the proceeds of the sale, less $100 commission, were credited to the Securities Corporation on petitioner's books (R. 45-7, 63, 158-160).

Respondent sold 2 shares of the stock in May 1932 (R. 23). He received three dividends paid respectively in January and July, 1931 and January, 1932 (R. 23).

On March 3, 1933, petitioner was closed by reason of the bank holiday and never reopened. It was then insolvent (R. 47). A conservator was appointed on March 13, 1933 and a receiver in November 1933* (R. 54).

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* The correct date of the receiver's appointment is October 16, 1933.

In May 1933, two months after the bank was closed and two and one-half years after respondent had acquired the stock, he read in a newspaper that an action had been brought by another stockholder charging fraud in the sale of shares of petitioner's stock (R. 26-27). Thereupon respondent tendered to the conservator the 8 shares of stock then owned by him and demanded payment of the purchase price (R. 29, 72). The conservator rejected the demand and the present action was begun on May 31, 1933 (R. 1).

The trial was had before a judge and jury. It was established that the shares which had been purchased by the respondent on the inducement of misrepresentations as to the value of the shares (R. 17-19) were not petitioner's property and that petitioner was not enriched by reason of the sale (R. 45-7).

When both sides rested, each moved for the direction of a verdict and the trial judge, to whom the determination of the facts was thus submitted by both parties, found that petitioner was not enriched by the sale of the stock to respondent and that the officers who dealt with respondent had no actual or apparent authority to make the representations in connection with the sale of the stock (R. 63).

Accordingly, he directed a verdict in favor of petitioner and its co-defendant. The respondent did not move to go to the jury on any question of fact (R. 63). Judgment was entered on the directed verdict (R. 12-3) and respondent appealed (R. 150-4).

The Circuit Court of Appeals, although apparently not questioning the finding that there had been no enrichment of petitioner, held that petitioner's officers who had made the fraudulent representations were clothed with actual or apparent authority so as to bind petitioner by their representations.

The Circuit Court of Appeals approved the rescission by respondent of the sale of the shares, thereby in effect requiring that the petitioner accept shares of its stock which it had never owned, and adjudged that respondent is entitled to recover the amount demanded in the complaint.

As petitioner did not attempt to rescind until May, 1933, after the bank had become insolvent and its doors were closed, the Circuit Court of Appeals held that he could not at that time "change his status from that of shareholder to that of creditor to the detriment of general creditors" (R. 161).

The result was that although the Circuit Court of Appeals held that "rescission should be allowed as against the corporation", it ruled that the judgment to be entered should "give the plaintiff no claim entitled to share in the assets of the receivership until after payment of all who were creditors when the bank became insolvent" (R. 162).

Accordingly, the judgment of the District Court was reversed and the order for mandate directed "that judgment for the amount demanded in the complaint be entered against the defendant, The Harriman Bank and Trust Company of the City of New York, collectible out of the assets of the receivership after payment in full of all who were creditors when the said bank became insolvent" (R. 178-9).

The Circuit Court of Appeals dismissed the action as to the conservator because a receiver for the bank had been appointed during the pendency of the action (R. 178).

II.

The Reasons Relied on for the Allowance of the Writ.

Petitioner believes that the writ of certiorari should be granted because:

(A) The Circuit Court of Appeals has directed that a claim founded upon the fraud of national bank officers in procuring the person defrauded to purchase shares of the bank's stock shall participate in the distribution of the proceeds of the stock assessment.

The question of the propriety of permitting qualified participation of such a claim in the proceeds of a stock assessment was reserved by this Court in *Lantry* v. *Wallace,* 182 U. S. 536. Doubt was cast upon the right to such qualified participation by the Circuit Court of Appeals in that case as follows: "It is questionable, to say the least, whether a judgment recovered against the bank for the alleged fraud and deceit could be permitted to participate in the distribution of the fund created by the stock assessment until all contract obligations of the bank had been fully paid", etc. (*Lantry* v. *Wallace,* 97 F. 865, at p. 870), but the question was not resolved because the cross demand for such participation could not be entertained in the action there involved.

The Circuit Court of Appeals has, therefore, decided an important question of Federal law in a way probably untenable and in conflict with the weight of authority, which question has not been, but should be, settled by this Court.

(B) The Circuit Court of Appeals by its judgment has directed petitioner to accept the ownership of certain shares of its stock which were not its property and thereby has compelled, in effect, a reduction of its outstanding capital stock. Since this ruling is applicable to going banks, it is of great importance to the proper administration of such institutions. The Circuit Court of Appeals has, therefore, decided an important question of Federal law which has not been, but should be, settled by this Court. In principle, the decision seems to be in conflict with the decision of this Court in *Awotin* v. *Atlas Exchange Nat. Bank*, 295 U. S. 209.

(C) The Circuit Court of Appeals, by the terms of its reversal of the judgment entered upon the verdict directed by the District Court, has held petitioner liable for the fraud of its officers in connection with the sale of shares of its corporate stock not among its assets but the property of another although it received no benefit from the transaction. In so holding, the Circuit Court of Appeals has proceeded upon the assumption that the officers of a national bank may impose liability upon it to a person purchasing shares of its stock though dealing in its stock is directly prohibited by specific provision of the National Banking Act. The Circuit Court of Appeals has, therefore, decided an important question of Federal law which has not been, but should be, settled by this Court.

WHEREFORE, your petitioner prays that a writ of certiorari issue to the United States Circuit Court of Appeals for the Second Circuit, commanding said Court to certify and send to this Court a full and complete transcript of the record and all proceedings

had in this cause, to the end that this cause may be reviewed and determined by this Court; that the judgment of said Court, reversing the judgment of the District Court, may be reversed, and that the petitioner be granted such other and further relief as may be meet and just.

Dated, New York, January 18, 1937.

THE HARRIMAN NATIONAL BANK AND TRUST COMPANY OF THE CITY OF NEW YORK,
By MARTIN CONBOY,
Counsel for Petitioner.

BRIEF IN SUPPORT OF PETITION FOR CERTIORARI.

Opinion in the Court Below.

The District Court filed no opinion. The grounds of its decision, stated orally from the bench at the close of the trial, appear at page 63 of the record.

The opinion of the Circuit Court of Appeals, reversing the judgment of the District Court, is reported in 85 F. (2d) 582, and appears in the record at pages 157-162.

Jurisdiction.

The judgment which is sought to be reviewed was entered November 9, 1936 (R. 178-9).

Jurisdiction to review this cause by writ of certiorari is conferred upon this court by section 240 (a) of the Judicial Code as amended by Act of February 13, 1925 (Title 28 U. S. C. §347 [a]).

Statement of the Case.

A statement of the case is set forth in the foregoing petition (pp. 2-4, *supra*).

Specification of Errors Intended to be Urged.

The Circuit Court of Appeals erred in the following respects:

1. In holding that a claim founded upon the fraud of national bank officers in procuring the person defrauded to purchase shares of the bank's stock shall participate in the distribution of the proceeds

of the stock assessment collected under the provisions of 12 U. S. C. Section 64 (Federal Reserve Act of December 23, 1913, Section 23 [38 Stat. 273]).

2. In holding that a national bank can be compelled to take and pay for and thereby acquire shares of its own capital stock in a manner unauthorized by Title 12, U. S. C. Section 83 (R. S. Section 5201) by invoking against the bank a right to rescind purchase of such shares from another than the bank through the fraud of the bank officers.

3. In holding that a national bank may be made liable for the fraud of its officers in connection with the sale of shares of its corporate stock which said shares were not sold from among its assets but were the property of another and the bank was not enriched by the transaction.

4. In holding that respondent is entitled to any recovery against petitioner.

Summary of Argument.

I.

The decision sought to be reviewed is erroneous because it directs that a claim founded upon the fraud of national bank officers in inducing the person defrauded to purchase shares of the bank's stock shall participate in the proceeds of an assessment collected from the other shareholders.

II.

The decision sought to be reviewed is erroneous because it compels petitioner, a national bank, to acquire and to pay for shares of its own capital stock in a manner unauthorized by Title 12, U. S. C., Section 83 (R. S. Section 5201), the only provision of law under which a national bank may acquire and hold shares of its own stock.

III.

The decision sought to be reviewed is erroneous because it imposes liability upon a national bank for the fraud of its officers in connection with the sale of shares of its corporate stock which said shares were not sold from among its assets but were the property of another and it was not enriched by the transaction.

Argument.

I.

The decision sought to be reviewed is erroneous because it directs that a claim founded upon the fraud of national bank officers in inducing the person defrauded to purchase shares of the bank's stock shall participate in the proceeds of an assessment collected from the other shareholders.

Petitioner is not a going bank. It is in receivership and has, since March 3, 1933, been insolvent (R. 47). The Comptroller of the Currency has levied an assessment against the stockholders in the full amount provided for by Title 12 U. S. C., Section 64 (R. 53). That section is as follows:

> "§64. *Individual liability of shareholder; transfer of shares.* The stockholders of every national banking association shall be held individually responsible for all contracts, debts, and engagements of such association, each to the amount of his stock therein, at the par value thereof in addition to the amount invested in such stock. The stockholders in any national banking association who shall have transferred their shares or registered the transfer thereof within sixty days next before the date of the failure of such association to meet its obliga-

tions, or with knowledge of such impending failure, shall be liable to the same extent as if they had made no such transfer, to the extent that the subsequent transferee fails to meet such liability; but this provision shall not be construed to affect in any way any recourse which such shareholders might otherwise have against those in whose names such shares are registered at the time of such failure (Dec. 23, 1913, c. 6, §23, 38 Stat. 273)."

The liability of the stockholders defined by the above section exists by virtue of the statute.

U. S. v. *Knox,* 102 U. S. 422.

Whenever a receiver appointed by the Comptroller of the Currency enforces as provided for in Title 12 U. S. C., Sections 191 and 192,* the personal liability of a shareholder of a national bank under Title 12 U. S. C., Section 64, he does not do so in the right of the bank.

Therefore, when the receiver sues to recover the assessment the shareholder may not offset against the assessment a claim that he had been defrauded by the bank in the acquisition of the stock. He may not thereby escape payment of the assessment that is made to meet the deficiency of assets.

Scott v. *Deweese,* 181 U. S. 202, 213;
Lantry v. *Wallace,* 182 U. S. 536, 549.

Consequently, when the defrauded stockholder seeks to obtain damages or restitution from the contributions of his fellow stockholders, something more is involved than the mere question whether he has been defrauded by the act of the corporation. The important question that is presented is whether he

* Set forth in full in Appendices A and B hereto, pages 33-34.

can, under the statute (12 U. S. C. §64), recover for such fraud from his innocent fellow shareholders.

The question has not yet been passed upon by this Court but it has been by the House of Lords. The Companies Act, 1862 (25 and 26 Victoria p. 614), contained a provision, Section 38, that made every present and past member of a company formed under the act liable to contribute to the assets of the company to an amount sufficient for payment of its debts and liabilities. The City of Glasgow Bank was incorporated under the Companies Act, 1862. One Houldsworth purchased £4,000 of the bank stock from the bank itself in February, 1877 at the price of £9,000. He was registered and received dividends. The bank went into liquidation in October, 1878, with immense liabilities and Houldsworth, as did the respondent in the case at bar, paid an assessment. He brought an action against the liquidators (corresponding to the receiver under our system) to recover damages in respect of the sum he had paid for the stock, in respect of the first call and in respect of the estimated future calls. He founded his claim upon the ground of fraudulent misrepresentations made by the directors and other bank officials to him. The Court of Session in Scotland dismissed his action. He appealed to the House of Lords. The following are from the opinions of the Law Peers:

> "Such an action of damages as the present is really not against the corporation as an aggregate body, but is against all the members of it except one, viz., the Pursuer; it is to throw upon them the Pursuer's share of the corporate debts and liabilities. Many of those shareholders (as was observed by Lord *Cranworth* in *Addie's Case* [L. R. 1 H. L., Sc. 145]) may have come and probably

did come into the company after the Pursuer had acquired his shares. They are all as innocent of the fraud as the Pursuer himself; if it were imputable to them it must, on the same principle, be imputable to Pursuer himself as long as he remains a shareholder; and they are no more liable for any consequences of fraudulent or other wrongful acts of the company's agent than he is. Rescission of the contract in such a case is the only remedy for which there is any precedent, and it is in my opinion the only way in which the company could justly be made answerable for a fraud of this kind. But for rescission the Appellant is confessedly too late."

Lord Selborne in *Houldsworth* v. *City of Glasgow Bank and Liquidators*, 5 App. Cas. 317, 329-30.

The very relief granted to the respondent in the instant case by the Circuit Court of Appeals was suggested in the lower court in the *Houldsworth* case and is thus dealt with by the Lord Chancellor (Earl Cairns):

"It appears to have been contended in the Court below that the Appellant might be unable to maintain the present action as a claim in the liquidation to be satisfied *pari passu* with other creditors, and yet might be able to maintain it as a claim against the company or against shareholders in the company after all other creditors were satisfied. In the argument at your Lordships' Bar I think it was felt to be impossible to maintain this theory of a deferred or secondary right of action against the company. I am satisfied there is no foundation for it. *The Winding-up Act* has no provisions for the payment of claims against the company except the claims of

creditors. Creditors are supposed to be paid *pari passu*, and there is no provision after they are paid for opening up fresh claims by a contributory against the company. There are, indeed, provisions which, after the debts are paid, enable any inequalities in the contributions of the contributories to be set right, but that is quite a different matter."

Houldsworth v. *City of Glasgow Bank and Liquidators*, 5 App. Cas. 317, at page 323.

At the beginning of the Lord Chancellor's opinion, he dealt with the fundamental question whether there could be repudiation of the stock after insolvency:

"It was admitted before your Lordships, as indeed it could not be denied, that after the winding-up of the company commenced it was too late for the Appellant to repudiate his stock, and that he must remain, as the liquidation found him, a partner in the bank and a contributory as such" (*do.*, pp. 322-323).

In the same case, Lord Hatherley expressed views on a situation with which the court was there concerned in all respects analogous to that involved in the instant case as follows:

"In truth the Appellant is trying to reconcile two inconsistent positions, namely, that of shareholder and that of creditor of the whole body of shareholders including himself. As has been observed already by those of your Lordships who have preceded me, amongst the various cases which have been brought before the Courts in respect of dealings with joint stock companies, no case can be adduced in which a person so claiming to be a shareholder has at the same

time successfully asserted his claim against a company in liquidation for such a debt as this, namely one in which he is himself a co-debtor with all his fellow shareholders to himself, and is himself in common with them responsible again to them individually for like liabilities irrespective of representations made by their common agent" (*do.*, pp. 333-4).

The principle stated in the *Houldsworth* case *supra* was applied by Sir George Jessel, Master of the Rolls, in *Re Hull and County Bank, Burgess's Case,* 15 Ch. Div. 507. There, a shareholder of a bank who had been induced by fraudulent misrepresentations contained in the prospectus to apply for shares attempted to rescind his contract and recover the sum paid for the shares after the bank had gone into liquidation. The Master of the Rolls, holding that such a claim might not be successfully asserted, said:

Page 512:

"Now, the other shareholders are as innocent of this fraud as the applicant. There is no pretense for saying that they authorized the committal of it; on the contrary, they themselves were defrauded in like manner. Therefore, they acquired rights as innocent parties under the 38th section which this applicant seeks to take away from them. It is quite true that in *Oakes* v. *Turquand** the only persons whose rights were decided upon were creditors, but the rights of other persons equally innocent were not required to be considered, because there was not enough to pay the creditors.

"In this case, however, it is said that the assets of the company contributed by the other

* L. R. 2 H. L. 325.

shareholders are sufficient to pay the creditors in full and all costs, and, therefore, that, the creditors having been paid or provided for, those rights are not to be considered; but, as I said before, the other contributories are also innocent persons, and have acquired rights, and I see no reason why those rights should not be considered."

The Master of the Rolls said (pp. 513-514):

"Therefore, if you have paid for your shares, and your payment has been applied in the payment of creditors, and the other contributories have not fully paid, they being equally innocent, you would be entitled on that theory to claim back the sum you had paid, and to have it paid you by a call on the other contributories. Of course that would not be enforcing the adjustment of the rights of the contributories amongst themselves, because, as I said before, these other contributories are not the persons who committed the fraud, and they are not liable, and, consequently, if you cannot have total rescission of the contract, it is plain you cannot have partial rescission either, and the claim must wholly fail."

See also:

East Broken Hills Consols., Ltd. v. *Mallaby-Deeley*, 11 T. L. R. 241, aff. id. 245.

In England, therefore, it is well established that after the statutory proceedings for winding up a corporation by reason of corporate insolvency have been commenced, the shareholder may not rescind his subscription on account of fraud. We are now to inquire whether there is anything in Title 12,

U. S. C., Section 64,* providing for assessments on shareholders that justifies the ruling by the Circuit Court of Appeals sought to be reviewed.

The recovery directed in favor of the respondent in the present case will of necessity come out of the assessment contributed by the stockholders of the bank. It cannot come out of the assets of the bank for the bank was concededly insolvent on March 3, 1933 (R. 47), and its assets are, therefore, insufficient to pay its creditors. In substance and effect the decision of the Circuit Court of Appeals makes the stockholders of the bank liable to satisfy respondent's claim out of the assessment which they are required to pay.

No such claim seems to be within the compass of the statute providing for the double liability of stockholders of national banks, and on reason therefore, the instant case should be ruled by the authorities cited.

The language of the statute is as follows:

> "The stockholders * * * shall be held individually responsible for all contracts, debts, and engagements of such association" etc.

Since, as we have seen, the liability of the shareholders is imposed by the statute, anyone asserting a right to share in the proceeds of the assessment must prove that his claim is one for which the shareholders are responsible. Whether the liability imposed on the shareholders be regarded as statutory or contractual, certainly it may not include risks which neither the statute contemplated nor the stockholders have undertaken.

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* Set forth in full, *supra*, pages 11-12.

In *Clinton Mining & Mineral Co.* v. *Beacom,* 266 F. 621 (C. C. A. 3); petition for a writ of certiorari denied, 254 U. S. 637, an action was brought by a judgment creditor of a South Dakota corporation against a stockholder of that corporation to enforce the stockholder's statutory liability for debts of the corporation. It was held that the defendant might go behind the judgment and if it had been obtained on a claim which was not comprised within the statutory liability the judgment creditor could not recover against the stockholder because the latter's liability depended on the nature of the claim against the corporation on which the judgment was founded.

In that case there was no such statutory context as results from the use in Title 12, U. S. C., Section 64, of the word "debts" between "contracts" and "engagements", indicating, under the familiar principle of *noscitur a sociis* that "debts" must be construed as obligations analogous to those arising out of contracts and engagements.

The language of the South Dakota statute was:

> "Each stockholder of a corporation is individually and personally liable for the debts of the corporation to the extent of the amount that is unpaid upon the stock held by him."

The judgment creditor who sought to collect the statutory liability from the stockholder had recovered a judgment in an action of tort against the corporation in which the defendant held stock. The Circuit Court of Appeals, in affirming judgment of non-suit, wrote as follows:

> "In legal dictionaries defining the word 'debt' the consensus of definition is to give the technical meaning of certainty of amount as the ear-

mark of a debt, and to contrast its specific promise by contract, with the uncertainty of general words such as 'obligation', 'liability', and the like. But not only does the word 'debt' carry with it the requirement of certainty and the foundation of promise by express contract, but it necessarily implies legality, since the basis of its obligation is legality based on promise and lawful consideration, and hence it will be seen that, a debt being in its nature certain, contractual, and lawfully incurred, it is reasonable that a statute should enact that a stockholder should be held liable for debts a corporation would properly and legally incur. From all of which it would clearly appear that both from the uncertainty and indefiniteness of uncontracted for liability, and from the illegality and wrong from which it arises, that a tort or wrong on the part of a corporation stands in a wholly different relation to a stockholder than does a debt with its certainty of contract and its legality of consideration.

The corporation has no right to commit such tort or wrong. When the stockholder subscribed for its stock, it was not with the purpose of creating an agency that should commit a tort or wrong. Such acts were not incident to purposes for which it was formed, nor was the liability for such wrong which inured to the one wronged thereby, a right for which the latter bargained in the course of what the corporation was impliedly authorized by the stockholder to do. On the contrary, the wrong done was a wrong illegally done by the corporation, not only to the third party, but a wrong done equally and illegally to its stockholder. Such being the case, he who would make the word 'debt' in this statute a synonym for tort, and thereby impose liability on the stockholder, is giving the word 'debt' an

effect which usage does not warrant nor reason justify. We are therefore of opinion that the tort of which the milling company was guilty in unlawfully mining the plaintiff's ore, was not a debt of the tort-feasor corporation, for which its stockholders were made personally liable by this statute."

Clinton Mining & Mineral Co. v. *Beachom,* 266 F. 621, 623.

It is petitioner's respectful submission that a claim founded upon the fraud of national bank officers in inducing the person defrauded to purchase shares of the bank's stock does not come within "contracts, debts, and engagements" within the meaning of Title 12, U. S. C. Section 64, and that it was error, therefore, for the Circuit Court of Appeals to order that such claim should participate in the proceeds of an assessment collected from the shareholders.

II.

The decision sought to be reviewed is erroneous because it compels petitioner, a national bank, to acquire and to pay for shares of its own capital stock in a manner unauthorized by Title 12, U. S. C., Section 83 (R. S. Section 5201), the only provision of law under which a national bank may acquire and hold shares of its own stock.

A national bank cannot purchase its own stock except to prevent loss previously contracted.

"Section 83. *Loans on or purchase by bank of own stock.* No association shall make any loan or discount on the security of the shares of its own capital stock, nor be the purchaser or holder of

any such shares, unless such security or purchase shall be necessary to prevent loss upon a debt previously contracted in good faith; and stock so purchased or acquired shall, within six months from the time of its purchase, be sold or disposed of at public or private sale; or, in default thereof, a receiver may be appointed to close up the business of the association, according to section 192 of this title."

12 U. S. C. Section 83 (R. S. §5201).

By the decision sought to be reviewed, the sale of shares of stock not owned by petitioner is rescinded as against petitioner, thereby making petitioner the owner of the stock.

The judgment sought to be reviewed, therefore, presents an important question of Federal law applicable to all national banks, including going concerns (R. 161).

The decision of the Circuit Court of Appeals creates an equivocal situation with respect to the capital stock of a national bank in conflict with the object and policy of the section just quoted.

"The object and policy of the statute in prohibiting a bank from purchasing outright its stock is to prevent the reduction of its outstanding stock, and the withdrawal *pro tanto* of its capital. *Bank* v. *Lanier,* 11 Wall. 374, 379."

Wallace v. *Hood,* 89 F. 11, 13.

"The transaction here in question was not a purchase made for the purpose of preventing, or which was necessary to prevent, loss upon a debt previously contracted, but, as set forth, it was a bald purchase by the bank of its own stock for cash, and necessarily involved for the time being

a reduction *pro tanto* of the corporate stock. Even if it were not forbidden by the statute, the transaction would be inconsistent with public policy and with established principles of law."

Burrows v. *Niblack,* 84 F. 111, 113-4 (C. C. A. 7).

Not only is a national bank prohibited from acquiring shares of its own stock except under the conditions defined by 12 U. S. C., Section 83, but it is also prohibited from withdrawing any portion of its capital, as is required by the decision of the Circuit Court of Appeals.

"Section 56. *Prohibition on withdrawal of capital; unearned dividends.* No association, or any member thereof, shall, during the time it shall continue its banking operations, withdraw, or permit to be withdrawn either in the form of dividends or otherwise any portion of its capital * * * but nothing in this section shall prevent the reduction of the capital stock of the association under Section 59 of this Article."

Title 12, U. S. C., Section 56 (R. S. §5204).

The only provision for reduction of capital is as follows:

"Section 59. *Reduction of capital by vote of shareholders.* Any association formed under this chapter may, by the vote of shareholders owning two-thirds of its capital stock, reduce its capital to any sum not below the amount required by this chapter to authorize the formation of associations; but no such reduction shall be allowable which will reduce the capital of the association below the amount required for its outstanding circulation, nor shall any reduction be made

until the amount of the proposed reduction has been reported to the Comptroller of the Currency and such reduction has been approved by the said Comptroller of the Currency and no shareholder shall be entitled to any distribution of cash or other assets by reason of any reduction of the common capital of any association unless such distribution shall have been approved by the Comptroller of the Currency and by the affirmative vote of at least two-thirds of the shares of each class of stock outstanding, voting as classes. (R. S. §5143; Dec. 23, 1913, c. 6, §28, 38 Stat. 274; Aug. 23, 1935, c. 614, §334, 49 Stat. 720.)"

Title 12, U. S. C., Section 59.

The purpose intended to be accomplished by the various statutory provisions relating to national banks is that at all times the bank's stock shall be fully paid and that the bank shall have outstanding the amount of its capital stock for the security of its creditors and for the transaction of its business.

"The bank president could not lawfully acquiesce in the attempted rescission. A surrender of the stock by appellee and an acceptance of it by the bank would have constituted an unauthorized reduction in the capital stock of the banking association. The capital stock of a national banking association may be reduced pursuant to Section 59, Title 12, U. S. C. A. and not otherwise."

Schechter v. *Sherwin,* 81 F. (2d) 603, 605 (C. C. A. 7).

See to the same effect:

Helburn Thompson Co. v. *All Americas Mercantile Corporation,* 211 App. Div. (N. Y.) 69.

The provisions of the statutes and the expressions of the court to which attention is directed under this point would seem to justify the following conclusions:

A national bank must have a fixed amount of stock, which must be paid in within six months after commencement of business (12 U. S. C., Sections 51, 51c, 53*). The aggregate of such stock represents the fund to which the creditors may look in the event of insolvency to cover deficiency in assets (*Id.*, Section 54†).

When the stock has been issued, the law contemplates that its quality of being outstanding shall not be affected otherwise than by the reduction to be accomplished under 12 U. S. C. Section 59, except where acquisition of shares is necessary to permit realization upon a debt owing to the bank contracted prior to such acquisition. In the parlance of the examining service, such transactions are known as D. P. C. (debts previously contracted). Even in a case falling within this category, the stock that is temporarily withdrawn must be put out again within six months under penalty of the closing up of the bank.

In this situation, a requirement that the bank shall accept shares of its own stock as the result of invoking the doctrine of rescission would seem to involve consequences neither permitted nor contemplated by the scheme of laws relating to national banks and in apparent violation both of their terms and policy.

Therefore, when demand was made upon the conservator to accept from the respondent, after insolvency of the bank, the shares of a prior owner other

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* Set forth in full in Appendices C, D and E hereto, pages 35-37.

† Set forth in full in Appendix F hereto, pages 37-38.

than the bank and pay the respondent the amount paid by him for such shares, it is manifest that the conservator could not legally comply with such demand, and it seems to be equally manifest that the court cannot compel such compliance.

An attempt to require this bank to take back its own shares was denied in *Goess* v. *Ehret,* 13 F. Supp. 630 (affd. on other grounds 85 F. [2d] 109). The language of the district court is as follows:

> "Defendant purchased 100 shares of the stock of the bank on certain misrepresentations made by Harriman. These shares of stock sold to the defendant were sold out of the Harriman Securities Corporation's Suspense Account. The amount of the price was credited to the Securities Corporation.
>
> "Defendant by way of relief requested that the bank take back the shares of its own stock and pay to the defendant the purchase price of these shares. This relief cannot be granted. *Awotin* v. *Atlas Exchange Nat. Bank,* 295 U. S. 209, 55 S. Ct. 674, 79 L. Ed. 1393.
>
> "The bank was not permitted to sell the stock. If it attempted to do so, the person dealing with it would have no recourse for any loss that might occur. There can be no relief in this case."
>
> *Goess* v. *Ehret,* 13 Fed. Supp. 630.

By this decision the district court assimilated an attempt to compel a national bank to retake its own shares to the effort to compel such a bank to retake securities which it had sold under a contract that violated Title 12, U. S. C. Section 24, Subdivision Seventh, as amended by the Act of February 25, 1927 (44 Stat. 1226, Section 2).*

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* Set forth in full in Appendix G hereto, page 38.

In *Awotin* v. *Atlas Exchange Nat. Bank,* 295 U. S. 209, attempt was made to avoid the definite prohibition contained in the statute by the claim that a quasi-contractual right could be based upon failure of consideration and also upon the theory of law which allows recovery where one party has been unjustly enriched at the expense of another.

Neither theory prevailed in the face of the direct prohibition in the statute itself against the marketing of obligations except "without recourse". There would seem to be little difference in principle between a definite prohibition of that character and that which is implicit in Title 12, U. S. C. Section 83, limiting the instances in which a national bank may acquire its own stock.

In this connection, we may properly quote from the opinion of this Court as follows:

> "National banks are public institutions, and the purpose and effect of the statute is to protect their depositors and stockholders and the public from the hazards of contingent liabilities, attendant upon the assumption by the bank of the risk of loss by its customers, resulting from the permitted dealing in securities by the bank. The prohibition would be nullified and the evil sought to be avoided would persist, if, notwithstanding the illegality of the contract to repurchase, the buyer, upon tender of the bonds, could recover all he had paid for them. Such a construction of the statute is inadmissible."
>
> *Awotin* v. *Atlas Exchange Bank,* 295 U. S. 209, 214.

III.

The decision sought to be reviewed is erroneous because it imposes liability upon a national bank for the fraud of its officers in connection with the sale of shares of its corporate stock which said shares were not sold from among its assets but were the property of another and it was not enriched by the transaction.

In *Jaskow* v. *Harriman Nat. Bank & Trust Company,* 159 Misc. (N. Y.) 39, the plaintiff sued to recover the sum of $3,030 as damages by reason of his purchase of two shares of the stock of The Harriman National Bank and Trust Company (petitioner) from the bank, claiming that such purchase had been induced by false representations made by a vice president of the bank.

The trial judge found that the stock was purchased by the plaintiff in the belief that he was purchasing it from the bank and not from The Harriman Securities Corporation (petitioner's affiliate) and that the stock was purchased in reliance upon false and fraudulent representations made by persons who were officers of the bank and also officers of the affiliate. Verdict was directed in favor of the defendants. The pertinent portions of the opinion of the trial court are as follows:

> "At the time of the transactions in question, it was entirely legal for the affiliate to buy and sell the shares of its affiliated bank but the bank had no authority to engage as principal in the business of buying and selling its own shares, such traffic being prohibited by the National Banking Act (U. S. Code, tit. 12, §83).
>
> "Plaintiff contends that the sale was made by the bank as principal and that the bank received

the proceeds or consideration thereof. On the record before me and within the period during which evidence as to the transactions was received, that is, from January to July, 1931, I reach the conclusion that the plaintiff has failed to sustain the burden of proof to establish that contention. * * *

* * * * * * *

"The purported sale of the stock by the bank and the representations by the persons who were bank officers in respect to the value of its shares were wholly unauthorized, and as against bank depositors and other creditors who concededly had nothing to do with the sale or the fraud in connection therewith, a bank stockholder should not on principle be allowed to recover, unless the consideration of the sale passed to the bank itself. The receipt of the proceeds is the only conceivable ratification of the transaction by the bank and this is the basis on which plaintiff in his bill of particulars sought to establish such ratification.

"It can never be assumed that an officer of a national bank had authority to transact business in which the bank, by its charter (as restricted by the Banking Act), was expressly prohibited from engaging. (*Alexander* v. *Cauldwell,* 83 N. Y. 480, 486.) The prohibitions of the act are primarily for the security of national banking institutions, that is, for the protection of depositors and other creditors; and if the bank has not received the proceeds of the unauthorized transaction the loss should not be inflicted upon it with the consequent impairment of financial responsibility.

"It has been repeatedly held that a national bank, contracting beyond its powers, is not liable for anything beyond what it received. (*Jack-*

man v. *Continental National Bank,* 16 F. (2d) 728; *Merchants Nat. Bank* v. *Boston State Nat. Bank,* 10 Wall. 604, and numerous other cases cited; U. S. Code Ann., tit. 12, Banks and Banking, §24, note 145.) Assuming, therefore, that the bank, acting through its officers, did itself purport to sell the stock (instead of being a conduit through which the company sold it, as I find on this record), the public policy of the National Banking Act, aimed to protect depositors, would forbid recovery by a defrauded purchaser of the stock as against the bank, unless the bank, with the knowledge of the fraud, retained the proceeds of the sale.

* * * * * * *

"Plaintiff has, of course, a good cause of action against the individual officers who perpetrated the fraud, but it is against them as individuals and not as officers of the bank."

Jaskow v. *Harriman Nat. Bank & Trust Co.,* 159 Misc. 39, 40-42.

The foregoing opinion by Justice Dore, now of the Appellate Division, Supreme Court, First Judicial Department, was followed by the district judge in the instant case (R. 63).

The *Jaskow* case was also followed and, it is justifiable to say, upon the same reasoning, although there are no reported opinions in the Supreme Court or Appellate Division, in the case of *Thomas Bradley, appellant,* v. *Harriman National Bank & Trust Company of the City of New York, respondent,* 247 App. Div. 876, where the statement of the nature of the case and the judgment are as follows:

"Action to recover $7,560 as damages for alleged fraud in the sale to plaintiff of five shares

of stock of defendant bank. Judgment dismissing the complaint at the close of case unanimously affirmed, with costs. No opinion. Present—Martin, *P. J.*, McAvoy, O'Malley, Townley and Glennon, *JJ.*"

The case was tried before Wasservogel, *J.* and after affirmance by the Appellate Division, application was made to that court for leave to go to the Court of Appeals and was denied (248 App. Div. 564). Likewise, application to the Court of Appeals for leave to appeal was denied (271 N. Y. 663).

To the same effect:

Heitman v. *Harriman,* 14 F. Supp. 282 (D. C., S. D. N. Y.).

In *Smith* v. *Tracy,* 36 N. Y. 79, an attempt was made to charge the owner of bank stock with liability for the representations of the president of the bank with whom the owner had left the stock for sale. Judgment in favor of the plaintiff was reversed by the Court of Appeals on the ground that the president of the bank had no authority to warrant the stock which his principal empowered him merely to sell, the property, bank stock, being of a description not usually sold with warranty.

See also:

U. S. v. *Bank of Columbus,* 21 How. 356;
Farmers' State Guaranty Bank v. *Cromwell,* 70 Okla. 199, 173 Pac. 826;
Morse on Banks and Banking, 6th Ed., Section 132.

It is, therefore, respectfully submitted that this case is one calling for the exercise by this court of

its supervisory powers in order that the erroneous rulings made by the Circuit Court of Appeals for the Second Circuit may be corrected and the general questions raised herein with respect to the affairs of national banks may be settled, and that to such an end a writ of certiorari should be granted and this court should review the decision of the Circuit Court of Appeals for the Second Circuit, insofar as the same reverses the judgment of the District Court in favor of the petitioner and orders the entry of final judgment against petitioner for the amount demanded in the respondent's complaint, and finally reverse it.

CONCLUSION.

The prayer of the petitioner, The Harriman National Bank and Trust Company of the City of New York, that a writ of certiorari issue should be granted.

Respectfully submitted,

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Of Counsel.

Appendix A.

Title 12 U. S. C. §191.

"Whenever any national banking association shall be dissolved, and its rights, privileges, and franchises declared forfeited, as prescribed in section 93, or whenever any creditor of any national banking association shall have obtained a judgment against it in any court of record, and made application, accompanied by a certificate from the clerk of the court stating that such judgment has been rendered and has remained unpaid for the space of thirty days, or whenever the comptroller shall become satisfied of the insolvency of a national banking association, he may, after due examination of its affairs, in either case, appoint a receiver who shall proceed to close up such association, and enforce the personal liability of the shareholders, as provided in section 192. (June 30, 1876, c. 156, §1, 19 Stat. 63.)"

Appendix B.

Title 12 U. S. C. §192.

"On becoming satisfied, as specified in sections 131 and 132 of this title, that any association has refused to pay its circulating notes as therein mentioned, and is in default, the Comptroller of the Currency may forthwith appoint a receiver, and require of him such bond and security as he deems proper. Such receiver, under the direction of the comptroller, shall take possession of the books, records, and assets of every description of such association, collect all debts, dues, and claims belonging to it, and, upon the order of a

court of record of competent jurisdiction, may sell or compound all bad or doubtful debts, and, on a like order, may sell all the real and personal property of such association, on such terms as the court shall direct; and may, if necessary to pay the debts of such association, enforce the individual liability of the stockholders. Such receiver shall pay over all money so made to the Treasurer of the United States, subject to the order of the comptroller, and also make report to the comptroller of all his acts and proceedings.

Provided, That the comptroller may, if he deems proper, deposit any of the money so made in any regular Government depositary, or in any State or national bank either of the city or town in which the insolvent bank was located, or of a city or town as adjacent thereto as practicable; if such deposit is made he shall require the depositary to deposit United States bonds or other satisfactory securities with the Treasurer of the United States for the safekeeping and prompt payment of the money so deposited: *Provided,* That no security in the form of deposit of United States bonds, or otherwise, shall be required in the case of such parts of the deposits as are insured under section 264 of this title. Such depository shall pay upon such money interest at such rate as the comptroller may prescribe, not less, however, than 2 per centum per annum upon the average monthly amount of such deposits. (R. S. §5234; May 15, 1916, c. 121, 39 Stat. 121; Aug. 23, 1935, c. 614, §339, 49 Stat. 721.)"

Appendix C.

Title 12 U. S. C. §51.

"After June 16, 1933, no national banking association shall be organized with a less capital than $100,000, except that such associations with a capital of not less than $50,000 may be organized in any place the population of which does not exceed six thousand inhabitants. No such association shall be organized in a city the population of which exceeds fifty thousand persons with a capital of less than $200,000, except that in the outlying districts of such a city where the State laws permit the organization of State banks with a capital of $100,000 or less, national banking associations now organized or hereafter organized may, with the approval of the Comptroller of the Currency, have a capital of not less than $100,000. No such association shall hereafter be authorized to commence the business of banking until it shall have a paid-in surplus equal to 20 per centum of its capital: *Provided,* That the Comptroller of the Currency may waive this requirement as to a State bank converting into a national banking association, but each such State bank which is converted into a national banking association shall, before the declaration of a dividend on its shares of common stock, carry not less than one-half part of its net profits of the preceding half year to its surplus fund until it shall have a surplus equal to 20 per centum of its capital: *Provided,* That for the purposes of this section any amounts paid into a fund for the retirement of any preferred stock of any such converted State bank out of its net earnings for such half-year period shall be deemed to be an addition to its surplus fund if, upon the retirement of such preferred stock, the amount so paid into such retirement fund for such period may then properly be carried to surplus. In any such case the con-

verted State bank shall be obligated to transfer to surplus the amount so paid into such retirement fund for such period on account of the preferred stock as such stock is retired. (R. S. §5138; Mar. 14, 1900, c. 41, §10, 31 Stat. 48; Feb. 25, 1927, c. 191, §4, 44 Stat. 1227; June 16, 1933, c. 89, §17 (a), 48 Stat. 185; Aug. 23, 1935, c. 614, §309, 49 Stat. 709.)"

Appendix D.

Title 12 U. S. C. §51c.

"The term 'common stock' as used in sections 51a to 51d of this title means stock of national banking associations other than preferred stock issued under the provisions of sections 51a to 51d of this title. The term 'capital' as used in provisions of law relating to the capital of national banking associations shall mean the amount of unimpaired common stock plus the amount of preferred stock outstanding and unimpaired; and the term 'capital stock', as used in sections 101 and 177 of this title, shall mean only the amount of common stock outstanding. (Mar. 9, 1933, c. 1, §303, 48 Stat. 5.)"

Appendix E.

Title 12 U. S. C. §53.

"At least 50 per centum of the capital stock of every association shall be paid in before it shall be authorized to commence business; and the remainder of the capital stock of such association shall be paid in installments of at least 10 per centum each, on the whole amount of the capital, as frequently as one installment at the end of each succeeding month from the time it shall be authorized by the Comptroller of the

Currency to commence business; and the payment of each installment shall be certified to the comptroller, under oath, by the president or cashier of the association. (R. S. §5140.)"

Appendix F.

Title 12 U. S. C. §54.

"Whenever any shareholder, or his assignee, fails to pay any installment on the stock when the same is required by section 53 of this title to be paid, the directors of such association may sell the stock of such delinquent shareholder at public auction, having given three weeks' previous notice thereof in a newspaper published and of general circulation in the city or county where the association is located, or, if no newspaper is published in said city or county, then in a newspaper published nearest thereto, to any person who will pay the highest price therefor, to be not less than the amount then due thereon, with the expenses of advertisement and sale; and the excess, if any, shall be paid to the delinquent shareholder. If no bidder can be found who will pay for such stock the amount due thereon to the association, and the cost of advertisement and sale, the amount previously paid shall be forfeited to the association, and such stock shall be sold as the directors may order, within six months from the time of such forfeiture, and if not sold it shall be canceled and deducted from the capital stock of the association. If any such cancellation and reduction shall reduce the capital of the association below the minimum of capital required by law, the capital stock shall, within thirty days from the date of such cancellation, be increased to the re-

quired amount; in default of which a receiver may be appointed, according to the provisions of section 192 of this title, to close up the business of the association. (R. S. §5141.)"

Appendix G.

Title 12 U. S. C. §24.

"Upon duly making and filing articles of association and an organization certificate a national banking association shall become, as from the date of the execution of its organization certificate, a body corporate, and as such, and in the name designated in the organization certificate, it shall have power——

* * * * * * * *

Seventh: To exercise by its board of directors, or duly authorized officers or agents, subject to law, all such incidental powers as shall be necessary to carry on the business of banking; by discounting and negotiating promissory notes, drafts, bills of exchange, and other evidences of debt; by receiving deposits; by buying and selling exchange, coin, and bullion; by loaning money on personal security; and by obtaining, issuing, and circulating notes according to the provisions of this title: *Provided,* That the business of buying and selling investment securities shall hereafter be limited to buying and selling without recourse marketable obligations evidencing indebtedness of any person, copartnership, association, or corporation, in the form of bonds, notes and or debentures, commonly known as investment securities, under such further definition of the term 'investment securities' as may by regulation be prescribed by the Comptroller of the Currency, * * *. (R. S. §5136, Feb. 25, 1927, c. 191, §2, 44 Stat. 1226.)"